

# INDEX

	Page
Opinions below .....	1
Jurisdiction .....	1
Question presented .....	2
Statute and regulations involved .....	2
Statement .....	3
Argument .....	7
Conclusion .....	13

## CITATIONS

### Cases:

<i>Beattie v. Commissioner</i> , 159 F. 2d 788 .....	13
<i>Commissioner v. Smith</i> , 324 U. S. 177, rehearing denied, 324 U. S. 695 .....	7
<i>Gillespie v. Commissioner</i> , 128 F. 2d 140 .....	13
<i>Hackett v. Commissioner</i> , 159 F. 2d 121 .....	12
<i>Hooker v. Hoey</i> , 27 F. Supp. 489, affirmed, 107 F. 2d. 1016 .....	9, 11
<i>Hubbell v. Commissioner</i> , 150 F. 2d 516 .....	12
<i>Oberwinder v. Commissioner</i> , 147 F. 2d 255 .....	12
<i>Old Colony Tr. Co. v. Commissioner</i> , 279 U. S. 716 .....	7
<i>Raymond v. Commissioner</i> , 114 F. 2d 140, certiorari denied, 311 U. S. 710 .....	13
<i>Ward v. Commissioner</i> , 159 F. 2d 502 .....	12
<i>Ware v. Commissioner</i> , 159 F. 2d 542 .....	13

### Statutes:

Internal Revenue Code:	
Sec. 22 (26 U.S.C. 1946 ed., Sec. 22) .....	2, 7, 10
Revenue Act of 1932, c. 209, 47 Stat. 169, Sec. 22 (b) (2) .....	10

### Miscellaneous:

Treasury Regulations 45, Art. 32 .....	8
Treasury Regulations 62, Art. 32 .....	8
Treasury Regulations 65, Art. 32 .....	8
Treasury Regulations 69, Art. 32 .....	8
Treasury Regulations 74, Art. 52 .....	8
Treasury Regulations 77, Art. 52 .....	8
Treasury Regulations 86, Art. 22 (a)-2 .....	8
Treasury Regulations 94, Art. 22 (a)-2 .....	8
Treasury Regulations 101, Art. 22 (a)-2 .....	8
Treasury Regulations 103, Sec. 19.22 (a)-2 .....	3, 7, 8
Treasury Regulations 111, Sec. 29.22 (a)-2 .....	8



# In the Supreme Court of the United States

OCTOBER TERM, 1948

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No. 501

FREDERICK JOHN WOLFE, PETITIONER

*v.*

COMMISSIONER OF INTERNAL REVENUE

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*ON PETITION FOR A WRIT OF CERTIORARI TO THE  
UNITED STATES COURT OF APPEALS  
FOR THE NINTH CIRCUIT*

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## **BRIEF FOR THE RESPONDENT IN OPPOSITION**

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### **OPINIONS BELOW**

The opinion of the Tax Court of the United States (R. 14-40) is reported in 8 T.C. 689. The *per curiam* opinion of the Court of Appeals (R. 111) is reported in 170 F. 2d 73.

### **JURISDICTION**

The judgment of the Court of Appeals was entered on October 12, 1948. (R. 112.) The petition for a writ of certiorari was filed on January 7, 1949. The jurisdiction of this Court is invoked under 28 U.S.C. 1254.

### QUESTION PRESENTED

Whether the monthly payments received by the taxpayer after his retirement from employment under the circumstances of this case constitute compensation for personal service within the meaning of Section 22 (a) of the Internal Revenue Code and the applicable Treasury Regulations, or annuities taxable under Section 22 (b) (2).

### STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code:

#### SEC. 22. GROSS INCOME.

(a) [as amended by Section 1 of the Public Salary Act of 1939, c. 59, 53 Stat. 574] *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service \* \* \* of whatever kind and in whatever form paid \* \* \*.

(b) *Exclusions from Gross Income.*—The following items shall not be included in gross income and shall be exempt from taxation under this chapter:

\* \* \* \*

(2) *Annuities, Etc.*—(A) \* \* \* Amounts received as an annuity under an annuity or endowment contract shall be included in gross income; except that there shall be excluded from gross income the excess of the amount received in the taxable year over an amount equal to 3 per centum of the aggregate premiums or consideration

paid for such annuity (whether or not paid during such year), until the aggregate amount excluded from gross income under this chapter or prior income tax laws in respect of such annuity equals the aggregate premiums or consideration paid for such annuity. \* \* \*.

\* \* \* \*

(26 U.S.C. 1946 ed., Sec. 22.)

Treasury Regulations 103, promulgated under the Internal Revenue Code:

SEC. 19.22 (a)-2. *Compensation for personal services.*—Commissions paid salesmen, compensation for services on the basis of a percentage of profits, commissions on insurance premiums, tips, pay of persons in the military or naval forces of the United States, retired pay of Federal and other officers, and pensions or retiring allowances paid by private persons or by the United States are income to the recipients \* \* \*.

#### STATEMENT

The facts as found by the Tax Court (R. 16-26) may be summarized as follows:

The taxpayer, a citizen of Canada, was a resident of England from 1931 to 1941, when he came to the United States. He filed an income tax return for the year 1941 in California. (R. 16.)

In 1902 the taxpayer entered the employ of an oil company (the Queen City Oil Company, Ltd.) which was afterwards absorbed by Imperial Oil

Company, Ltd. (hereafter referred to as Imperial), a Canadian company, the stock of which was largely held by Standard Oil Company of New Jersey (hereafter referred to as Standard). (R. 16.) In 1931 the taxpayer was requested by an officer of Imperial to go to England to take over the duties of the managing director of the Anglo-American Oil Company, Ltd. (hereafter referred to as Anglo), an English corporation. Anglo was controlled by the Standard Oil Export Corporation, which in turn was controlled by Standard. (R. 16-17.) Before accepting the appointment with Anglo, the taxpayer conferred with officers of both Standard and Standard Oil Export Corporation. (R. 17.)

It was agreed when the taxpayer undertook the assignment of chairman and managing director of Anglo, at the request of Standard, that if he eventually was retired from the service of Anglo he would receive a life annuity based on the provisions of the superannuation scheme of Anglo in effect on the date of retirement and that payment of such pension in sterling would be guaranteed by Standard in dollars at an exchange rate of \$5 to the pound. (R. 17.)

In October, 1931, the board of directors of Anglo passed the following resolution (R. 19):

Resolved, it being part of the arrangement with Mr. Wolfe on his joining the Board of this Company, and becoming Managing Di-

rector, that for the purpose of calculating pension payable by this Company to him, his services shall be deemed to commence from June, 1902, on which date he joined the Queen City Oil Co., Ltd., (which was subsequently absorbed by the Imperial Company, Ltd., of Canada) and that he be entitled to pension on the same basis as employees benefiting under the Company's Superannuation Scheme dated 31st December, 1925, or any subsequent modification thereof.

In 1939 the taxpayer informed Anglo that he wished to retire and live in the United States and wanted his annuity to be paid in United States dollars at \$5 to the pound. Various procedures for paying the taxpayer were discussed by Standard, Anglo, and the taxpayer. Among them was a proposal to purchase an annuity from a commercial insurance company, which however was rejected. (R. 19.)

In June, 1939, the officers of Standard took under consideration the payment of the taxpayer's "annuity", payable in United States dollars and converted at the rate of \$5 to the pound. It was proposed that "the annuity be paid by New York in dollars" (R. 20); and in view of the uncertainties of the future <sup>1</sup> and in order to assure that the necessary funds be available in New York when needed, it was further proposed that Anglo trans-

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<sup>1</sup> World War II started about two months after the proposal in question was made.

fer to Standard the estimated present value of Anglo's liability (R. 21). In August, 1939, Anglo paid Standard £87,177-0-0 which were converted into \$408,097.33 in United States currency, and in December, 1939, Anglo paid Standard £1,943-0-0, which were converted into \$7,689.42 in United States currency. The sum of the two payments is £89,120-0-0, or \$415,786.76 at the then current rate of exchange (which was less than \$5). (R. 26.)

The three parties entered into an agreement dated March 22, 1940, which recites that the taxpayer undertook the assignment of managing director of Anglo at the request of Standard on the understanding that if he eventually were retired from the service of Anglo he would receive a life annuity based on the provisions of the superannuation scheme of Anglo and that payment of such sterling pension would be guaranteed by Standard in dollars at an exchange rate of \$5 to the pound. (R. 23-24.) The agreement provided that Anglo was to contribute to Standard £89,120-0-0, with the understanding that Standard was to pay the taxpayer \$3,038.75 per month for the rest of his life, and the same amount to his wife for the year following his death if she survived him, and that the taxpayer accepted this annuity as a complete discharge of any and all pension obligations of Standard, Anglo, and any other associated companies. (R. 24-25.)



The taxpayer retired from Anglo on July 1, 1940, and thereafter received \$3,038.75 per month from Standard which withheld the income tax on the monthly payments. (R. 26.) The taxpayer came to the United States on October 4, 1941 (R. 16), and received about \$8,800 for the balance of the year 1941, but reported in his income tax return only about \$3,000.<sup>2</sup> (R. 11.) The Commissioner determined a deficiency on the ground that the entire amount of about \$8,800 constituted income. (R. 11.) The Tax Court upheld the Commissioner and the court below affirmed the decision of the Tax Court *per curiam*. (R. 40, 111.)

#### ARGUMENT

1. The decision of the court below, affirming *per curiam* the decision of the Tax Court, is correct. Section 22 (a) of the Internal Revenue Code, as amended, *supra*, provides that gross income includes compensation for personal service of whatever kind and in whatever form paid. This Court has placed a broad construction on this provision of the statute. *Commissioner v. Smith*, 324 U. S. 177, rehearing denied, 324 U. S. 695; *Old Colony Tr. Co. v. Commissioner*, 279 U. S. 716. Section 19.22 (a)-2 of Treasury Regulations 103, *supra*, p. 3, explaining Section 22 (a) of the statute, pro-

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<sup>2</sup> The taxpayer made his return on the theory that the monthly payments were annuities, and consequently under Section 22 (b) (2) of the Internal Revenue Code, he was taxable only on 3% of the purchase price of the annuity, which he considered to be \$415,000. (R. 71.)

vides in part that pensions or retiring allowances constitute income to the recipients. A similar provision has been in the Treasury Regulations since 1921.<sup>3</sup> The statutory provision defining gross income, to which the Regulations refer, having been repeatedly reenacted in substantially the same form, the Regulations now have the force and effect of law.

Applying these Regulations to the facts of this case, it is clear that the disputed sum constitutes a taxable pension or retiring allowance paid to petitioner. Within eight months from the time the taxpayer assumed his duties as managing director of Anglo in March, 1931, the board of directors of that company passed a resolution providing that he was entitled to a pension on the same basis as employees benefiting under the company's super-

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<sup>3</sup> Article 32 of Treasury Regulations 45 (1920 ed.), promulgated under the Revenue Act of 1918, of Treasury Regulations 62 (1922 ed.), promulgated under the Revenue Act of 1921, of Treasury Regulations 65, promulgated under the Revenue Act of 1924, and of Treasury Regulations 69, promulgated under the Revenue Act of 1926; Article 52 of Treasury Regulations 74, promulgated under the Revenue Act of 1928, and of Treasury Regulations 77, promulgated under the Revenue Act of 1932; Article 22 (a)-2 of Treasury Regulations 86, promulgated under the Revenue Act of 1934, of Treasury Regulations 94, promulgated under the Revenue Act of 1936, and of Treasury Regulations 101, promulgated under the Revenue Act of 1938; Section 19.22 (a)-2 of Treasury Regulations 103, promulgated under the Internal Revenue Code; and Section 29.22 (a)-2 of Treasury Regulations 111, promulgated under the Internal Revenue Code.

annuation scheme dated December 31, 1925, and that for the purpose of calculating the pension payable by that company to him, his services should be deemed to commence from June, 1902. (R. 19.) It was this resolution which gave rise to the taxpayer's right to a pension from Anglo and which determined the basis upon which the pension would be paid. Due to the fact that Standard guaranteed the payment of the pension in dollars at \$5 to the pound (R. 17) and that the taxpayer wanted to live in the United States after his retirement and to be paid in United States dollars (R. 19), arrangements were made between Standard and Anglo whereby the latter in 1939 paid the former £89,-120-0-0 (R. 26), and the former undertook to pay the taxpayer \$3,038.75 per month, effective July 1, 1940, for the rest of his life and a similar amount to his wife for twelve months following his death if she survived him (R. 24-25). There is no evidence in the record to show that Anglo would not have paid the taxpayer his pension in sterling if he had continued to live in England, nor is there any evidence that the taxpayer contributed or agreed to contribute one penny to the pension or retirement fund of either Anglo or Standard. In short, we have a case which fits squarely into the provision that pensions or retiring allowances constitute income to the recipient.

*Hooker v. Hoey*, 27 F. Supp. 489 (S.D.N.Y.) affirmed *per curiam*, 107 F. 2d 1016 (C.A.2d), in-

volves circumstances similar to those in this case. The taxpayer, an employee of Vacuum Oil Company, retired from active service in 1924, and by resolution of the board of directors was awarded \$937.50 monthly, or \$11,250 yearly, for the rest of his life. The taxpayer received \$11,250 annually from his former employer from 1924 to 1931. In 1931, Vacuum Oil Company sold all its property to Standard Oil Company of New York, which assumed all obligations and liabilities of Vacuum. Thereafter, Standard made the payments to the taxpayer, including the sum of \$11,250 paid in 1933 which the taxpayer claimed was exempt from income tax on the ground that it was an annuity.<sup>4</sup> The District Court decided, and was affirmed *per curiam*, that the sum in question constituted income for 1933 because it was a pension or retirement allowance under the statute and the applicable Treasury Regulations; and the fact that Standard took over Vacuum and made the payments after 1931 was held immaterial. While no specific sum of money passed from Vacuum to Standard in the

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<sup>4</sup> Under Section 22 (b) (2) of the Revenue Act of 1932, c. 209, 47 Stat. 169, none of the amounts received under an annuity contract were treated as income until after the annuitant recovered his premium or other consideration. Under Section 22 (b) (2) of the Internal Revenue Code, *supra*, however, 3% of the total cost of the premium is included in taxable income, and the balance of the annual payments is excluded until the amounts excluded equal the cost of the annuity, after which all of the annual payments are included in gross income.

*Hooker* case comparable to the sum of \$415,000 which Anglo paid to Standard in this case, it was argued in that case that assets equivalent to the worth of an annuity of \$11,250 to a man 68 years of age (i.e. \$79,186.46) were transferred in consideration of Standard's promise to pay the "annuity". Nevertheless, the court correctly held that the taxpayer received a pension and not an annuity in the *Hooker* case, and it would follow that the taxpayer received a pension, rather than an annuity, in the instant case; the taxpayer did not contribute to the pension fund in either case and therefore had no cost to recover.

The taxpayer argues that the basic legal question presented by this case is whether the contract of March 22, 1940, resulted in the receipt of income in the amount of \$415,000 by the taxpayer in 1940, and that if this be so the monthly payments can only be taxed under Section 22(b)(2). (Pet. 29-30.) But he did not report this sum as income to any country in 1940 (R. 26, 38), and to say that he realized income in the amount of \$415,000 by reason of the execution of the contract finds no warrant whatsoever in the record. The only purpose of the contract of March 22, 1940, was to arrange for the payment of the taxpayer's pension in New York in dollars. The resolution passed by Anglo's board of directors on October 22, 1931, fixed the taxpayer's right to a pension and the date on which his services were deemed to commence. (R. 19.) Prior to that

time, Standard guaranteed the rate of exchange, namely, \$5 to the pound, at which the pension would be paid. (R. 17.) If the taxpayer had remained in England after his retirement, it is reasonable to assume that the contract of March 22, 1940, would never have been entered into; its sole purpose was to arrange for the payment of the pension in the United States and in dollars, and to fix the rate of exchange, namely, \$5 to the pound.

2. There is no conflict of decisions. The taxpayer asserts a conflict between the decision in the instant case and *Hackett v. Commissioner*, 159 F. 2d 121 (C.A.1); *Oberwinder v. Commissioner*, 147 F. 2d 255 (C.A.8); *Hubbell v. Commissioner*, 150 F. 2d 516 (C.A.6); and *Ward v. Commissioner*, 159 F. 2d 502 (C.A.2). (Pet. 10, 16-18.) In all of those cases, the employer purchased an admitted annuity contract from an insurance company for the benefit of an employee still in service, and it was held that the premiums paid for the annuity constituted income to the employee on the theory that they were in the nature of additional compensation. In this case, the taxpayer retired in accordance with an established plan, and it could not reasonably be said that he received a bonus of \$415,000, when his annual salary was £11,000 (\$55,000) (R. 23, 67), and he worked only six months in the year of his retirement (R. 26). In none of those cases did the employer set up a well defined pension plan as did Anglo in this case, and in none of them

was it urged that the installment payments were anything but true annuities.

The taxpayer also asserts a conflict with *Ware v. Commissioner*, 159 F. 2d 542 (C.A.5); *Beattie v. Commissioner*, 159 F. 2d 788 (C.A.6); *Raymond v. Commissioner*, 114 F. 2d 140 (C.A.7), certiorari denied, 311 U. S. 710; and *Gillespie v. Commissioner*, 128 F. 2d 140 (C.A.9) (Pet. 11, 19). In none of these cases, also, was it contended, as here, that the annual payment made to the taxpayer was a pension, rather than an annuity; in fact, in none of these cases was the annuitant a former employee, nor had he rendered any pensionable service. They are substantially different from the instant case on their facts.

#### CONCLUSION

The decision of the court below is correct and there is no conflict of decisions. The case depends largely upon its peculiar facts. The petition for a writ of certiorari should be denied.

Respectfully submitted,

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FEBRUARY, 1949.